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SUBJECT: MADAGASCAR: AMBATOVY MINING PROJECT UPDATE

11. (SBU) Summary: Despite dual financial and political crises, the USD 4.5 billion Ambatovy nickel mining project in eastern Madagascar is moving forward, with production scheduled to begin in early 2011. Ambatovy managers are able to work with the transition government (HAT), notwithstanding the HAT's occasional harassment of the company, but the project has suffered administrative delays due to mid-level staffing gaps at key ministries. The loss of technical capacity in the HAT is likely to worsen by year-end when World Bank funds for environmental assessments will be exhausted. A joint venture with Canadian, Korean, and Japanese partners, Ambatovy intends to forge ahead as quickly as possible so that it may begin repaying its several billion dollar debt. Despite an increasingly lawless Malagasy business climate, Ambatovy never experienced security problems through the recent crisis, only evacuated one employee among 10,000 (who returned in April), and is managing its day-to-day operations without particular difficulty. End summary.

Ambatovy Chugs Along Despite Financial Crisis

12. (SBU) The Ambatovy joint venture, 40 percent held by Canadian firm Sherritt, 27.5 percent each by Japanese Sumitomo and Korea Resources Corporation (Kores), and 5 percent by Canadian SNC Lavalin, is the largest foreign investment in Madagascar's history. Ambatovy's Environmental Director Pierre Berner told Emboff June 12 that the nickel and cobalt mine, pipeline, and refinery will amount to a USD 4.5 billion investment by the time production begins in early 12011. The companies have invested USD 3.8 billion to date and have borrowed over USD 2.5 billion. Ambatovy has been hard hit by the international credit crunch, and its stock, valued at USD 17 per share in early 2008 is currently only selling for USD 5.5. Sherritt, which is owed money by the Cuban government on its mining operations there, is "broke", Berner said. Sherritt, however, struck a deal with Kores and Sumitomo, in which those two companies, mainly Kores, agreed to pony up the additional funds needed to continue the project, while Sherritt maintains its 40 percent ownership. Berner suspected that Sherritt would have to pay them back in the future. Although the project has had to slow down and cut its budget wherever possible, Berner said that he thought they would be able to make it through these lean times.

. . . And Despite Malagasy Crisis

13. (SBU) Although the transition authority (HAT) has been saber-rattling about renegotiating mining contracts, Berner

does not think that the HAT will actually take concrete steps against Ambatovy, which is providing the government much needed tax revenue. Furthermore, the Ambatovy investment is based on the terms of Madagascar's mining law and a government decree implementing the law, rather than a contract between the company and the government. (Note: We and other embassies, as well as the World Bank and IMF, have stressed the importance of the HAT respecting contracts and commitments made previously by the government of Madagascar. End note.) The new Minister of Environment Mariot Jean Florent Rakotovoao was formerly a Sherritt employee; Berner explained that he had wasted about USD 30,000 of company money on nepotistic hiring and a shady housing loan program for his cronies and finally tried to force Sherritt to fire him and pay severance by taking six weeks leave after claiming to slip in his shower. He was, however, forced to resign himself after being offered the post of HAT environment minister. Despite these events (not the first time Rakotovoao has been fired from a job for corruption or incompetence), Berner maintains a good working relationship with him, but is unable to get needed permits for operations such as laying pipe under a national road due to the lack of mid-level staff at the ministry. The quasi-independent environment office (ONE), which oversees environmental requirements for mining and oil companies, continues to function under pre-existing leadership, but will run out of World Bank funds by year-end. The environment ministry made a grab for ONE, whose consulting positions are better paid than those of the ministry, but was deterred for the time being. The HAT has yet to name a minister of mines, but working-level staff are in place at the office of mines.

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¶4. (SBU) Given the prevailing lawlessness of the business atmosphere inspired by the coup and weak government, Ambatovy has been facing more employee strikes. Currently its contract workers from the French-owned Colas road construction firm are on strike due to the firing of one of their workers, who had been caught driving drunk. Ambatovy has not been affected significantly by the recent strike at the Tamatave container port, as it has its own bulk loading area that has continued to operate. It also has its own thermal electricity generation capacity, so its operations should not be impacted by the ongoing demise of the state electricity company (JIRAMA).

¶5. (SBU) Overall, Ambatovy operations have been more affected by the international financial crisis than local problems. Out of the company's approximately 10,000 contracted and direct hire employees, only one contract employee was evacuated during the crisis, and has subsequently returned. Family members were given the option to leave, but returned in April. The lack of tourists near the mine site actually was viewed by Sherritt as a positive impact as it alleviated traffic concerns near the site, and spared it complaints that may have arisen due to the actions (molesting women and violating traffic agreements) of a renegade Libyan contractor, which Sherritt has since fired.

Future Concerns

¶6. (SBU) Ambatovy is concerned about the negative repercussions that may come from laying off 8,000 (mostly construction) workers to downsize to a permanent workforce of approximately 2,000 after operations begin in early 2011. It will be difficult for the local economy to absorb or place these displaced workers. Berner also expressed concern about the multiple parts of the operation (pipeline, mine, refinery, delivery trucks, etc.) all working seamlessly together, particularly if the threat of strikes becomes more common. With the price of nickel at only around USD 7 per pound, the project's directors and creditors keep pushing managers to tighten their belts. With over USD 2.5 billion of debt, each day of delay repaying lenders equals a significant sum in interest payments. Along with these

financial pressures, Ambatovy is also worried about the possibility of the HAT changing the mining law implementing decree, however unlikely that may be.

Comment

¶7. (SBU) The Central Bank has been intervening on the foreign exchange market to prop up the Malagasy currency for several months. The Bank has been promoting a strong ariary in order to keep import prices, and inflation, low. This policy favors urban consumers at the expense of exporters and farmers. The additional USD 700 million investment inflow for the Ambatovy project expected over the next 18 months could put new upward pressure on the Malagasy currency, alleviating the Bank's perceived need for intervention. End comment.
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